

Catholic University Law Review

Volume 36
Issue 4 *Summer 1987*

Article 6

1987

Commentary

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Recommended Citation

Thomas L. Hazen, *Commentary*, 36 Cath. U. L. Rev. 987 (1987).
Available at: <https://scholarship.law.edu/lawreview/vol36/iss4/6>

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COMMENTARY

*Thomas Lee Hazen**

This symposium issue includes a number of interesting and provocative articles. Professor Karmel explores the basis for the Securities and Exchange Commission's power to regulate substantive shareholder voting rights. Commissioner Cox and Mr. Michael discuss the internationalization of the securities markets. Professor Carney questions the legitimacy of the SEC's increased emphasis on the enforcement of insider trading sanctions. Finally, Professor Lipton describes the scope of federal regulation of broker-dealers. The essay that follows provides a commentary on each of these articles.

I. KARMEL ON DUAL CLASS CAPITALIZATION AND DISPARATE VOTING RIGHTS

The federal securities laws are aimed primarily at full disclosure.¹ Corporate chartering laws, which are enacted in every state, apply to internal corporate affairs and corporate governance generally. While the focus of the federal law is on investor protection, state corporate laws approach shareholder protection from the vantage point of the shareholders' proprietary interests.² Over the course of its history, the Securities and Exchange Commission (SEC or the Commission) has made various inroads into the field of corporate governance.³ The most prominent SEC involvement in corporate governance is through the proxy regulation of publicly traded companies.⁴

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1. See, e.g., H. CHERRINGTON, *THE INVESTOR AND THE SECURITIES ACT* (1942); 1 L. LOSS, *SECURITIES REGULATION* 121-29 (2d ed. 1961); Douglas & Bates, *The Federal Securities Act of 1933*, 43 YALE L.J. 171 (1933); Landis, *The Legislative History of the Securities Act of 1933*, 28 GEO. WASH. L. REV. 29 (1959).

2. See Hazen, *Corporate Chartering and the Securities Markets: Shareholder Suffrage, Corporate Responsibility and Managerial Accountability*, 1978 WISC. L. REV. 391.

3. See, e.g., Jennings, *Federalization of Corporation Law: Part Way or All the Way?*, 31 BUS. LAW. 991 (1976). The increasing concern over defensive tactics to takeovers may spark a renewed interest in a federal corporation law. See Karmel, *Will Takeover Abuses Lead to Federal Corporation Law?*, N.Y.L.J., Feb. 19, 1987, at 1, col. 1.

4. 15 U.S.C. § 78n (1982); see E. ARANOW & H. EINHORN, *PROXY CONTESTS FOR CORPORATE CONTROL* (2d ed. 1968); T. HAZEN, *THE LAW OF SECURITIES REGULATION* §§ 11.1-11.9 (1985 & 1987 Supp.); 2 L. LOSS, *supra* note 1, at 857-1036.

Due to the dichotomy between the relative roles of federal securities law and state corporate law, each SEC foray into corporate governance raises questions as to whether a proper balance is being maintained. In the 1970's, the focus of the SEC was on shareholder access to the proxy machinery⁵ and the activities of corporate directors.⁶ In the 1980's, the Commission's attention has turned to the takeover arena generally and, in particular, to various management responses to anticipated and pending takeover attempts. Professor Karmel examines a very important aspect of this development: the regulation of shareholder voting rights in the context of dual class voting shares.⁷ Professor Karmel presents a thorough examination of the SEC's role and concludes that although the SEC has the power to regulate substantive voting rights, it should do so cautiously and reluctantly.

A major issue in recent years has been the ability of the management of public corporations to authorize a class of shares with weighted voting rights. Establishing a class of shares with superior voting rights has evolved as an increasingly popular defensive response to hostile takeover attempts. For most of its history, the New York Stock Exchange (NYSE) has prohibited the listing of shares where the issuer has a class of shares with disparate voting rights.⁸ Although the American Stock Exchange permits disparate voting rights within limits, it prohibits nonvoting common stock.⁹ The National Association of Securities Dealers (NASD) has no regulation of disparate voting rights at the present time, but it has proposed adoption of a one-share/one-vote rule.¹⁰

A number of companies have authorized stock in violation of the NYSE rule which led to a moratorium on its enforcement.¹¹ After considering the

5. See Black, *Shareholder Democracy and Corporate Governance*, 5 SEC. REG. L.J. 291 (1978); Schwartz & Weiss, *An Assessment of the SEC Shareholder Proposal Rule*, 65 GEO. L.J. 635 (1977).

6. See generally Ferrara, Starr & Steinberg, *Disclosure of Information Bearing on Management Integrity and Competency*, 76 NW. U.L. REV. 555 (1981).

7. Karmel, *Qualitative Standards for "Qualified Securities": SEC Regulation of Voting Rights*, 36 CATH. U.L. REV. 809 (1987).

8. N.Y.S.E. LISTED COMPANY MANUAL §§ 312.00, 313.00 (1984).

9. *American Stock Exchange Listing Standards, Policies and Requirements* § 122, 1 Am. Stock Ex. Guide (CCH) ¶ 10,022 (1985).

10. See NASD *Proposes Voting Rights Rule for all Major Equity Stock Markets*, 19 Sec. Reg. & L. Rep. (BNA) 399 (Mar. 20, 1987). It is interesting to note that a commissioned study by Professor Fischel concluded that the NASD should not require voting stock. See Karmel, *supra* note 7, at 820 n.76. However, the NASD is proposing listing requirements that would affect corporate governance such as a requirement for independent directors. *Id.* at 821. The current proposals are fraught with controversy; see, e.g., *Exchange Talks on One Share, One Vote Begin; Investors Slam NASD Plan*, SEC. WEEK, Mar. 30, 1987, at 5.

11. See NYSE *Initial Report of the Subcomm. on Shareholder Participation and Qualitative Listing Standards, "Dual Class Capitalization"* (Jan. 3, 1985).

rule, the NYSE proposed a reversal of its long-time position by permitting dual class capitalization, at least when approved by independent directors and the shareholders.¹² It seems ironic that the NYSE is moving away from its voting rights rule while the NASD has been moving toward adoption of such a rule. Because of the SEC's oversight responsibility with regard to self-regulatory organizations such as the NYSE and NASD,¹³ any such rule change must be approved by the SEC. The developments ushered in by management entrenchment tactics and the NYSE's proposed changes have spurred discussion as to the scope of the SEC's power to regulate substantive shareholder voting rights.

There has been considerable controversy with regard to the propriety of SEC regulation of shareholder voting rights that traditionally fall within the domain of state corporate law.¹⁴ As Professor Karmel points out, the primary thrust of the federal securities laws is disclosure, as opposed to regulation, of normative corporate behavior and governance patterns.¹⁵ While the SEC's mission is to protect the shareholders' interest as investors, the role of protecting the shareholders' proprietary interest in the corporation has been a matter of state law,¹⁶ notwithstanding numerous suggestions to federalize corporate law.¹⁷ On the other hand, section 14 of the Securities Exchange Act of 1934¹⁸ regulates the proxy machinery of publicly traded companies. As Professor Karmel notes, this section evidences a strong congressional recognition that shareholder suffrage plays an important role in investor protection.¹⁹ Furthermore, the proxy related disclosure obligations arguably are

12. See NYSE "Reluctantly" Adopts Dual Share Classification; SEC Approval Needed, 18 Sec. Reg. & L. Rep. (BNA) 998 (July 11, 1986).

13. Securities Exchange Act, 15 U.S.C. § 78s(b) (1982); see T. HAZEN, *supra* note 4, § 10.2.

14. See, e.g., Dent, *Dual Class Capitalization: A Reply to Professor Seligman*, 54 GEO. WASH. L. REV. 725 (1986); cf. Ratner, *The Government of Business Corporations: Critical Reflections on the Rule of "One Share, One Vote,"* 56 CORNELL L. REV. 1 (1970) (suggesting that major shareholders be granted only limited voting rights); Compare Seligman, *Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy*, 54 GEO. WASH. L. REV. 687 (1986) (arguing in favor of the Commission's authority) and Karmel, *The SEC's Power to Regulate Shareholder Voting Rights*, N.Y.L.J., Aug. 21, 1986, at 1, col. 1 with D. FISCHER, *ORGANIZED EXCHANGES AND THE REGULATION OF DUAL CLASS COMMON STOCK* (1986) (arguing against the efficacy of one share/one vote in maximizing shareholders' interests).

15. Karmel, *supra* note 7, at 811.

16. See Hazen, *supra* note 2.

17. See, e.g., Berlack, *Federal Incorporation and Securities Regulation*, 49 HARV. L. REV. 396 (1936); Cary, *A Proposed Federal Corporate Minimum Standards Act*, 29 BUS. LAW. 1101 (1974); Schwartz, *Federal Chartering of Corporations: An Introduction*, 61 GEO. L.J. 71 (1972).

18. 15 U.S.C. § 78n (1982).

19. Karmel, *supra* note 7, at 824.

based on the premise that shareholders of publicly traded companies have significant voting rights.²⁰ Professor Karmel carefully reviews both the history and text of the federal securities laws and concludes that the SEC has "significant substantive power to regulate the relationship between the managements of public corporations and their shareholders."²¹ She further traces the SEC's pattern of involvement in corporate governance and concludes that although the Commission has the authority to regulate shareholder voting rights, it should proceed "cautiously and formulate a . . . policy with extreme reluctance."²²

In addition to the federal proxy regulation, which is focused on disclosure and thus does not address directly the treatment of substantive voting rights, section 19(c) of the Securities Exchange Act provides the SEC with residual power to promulgate rules it "deems necessary or appropriate to insure the fair administration of the self-regulatory organization, to conform its rules to requirements of this chapter . . . in furtherance of the purposes of this chapter"²³ It has been argued, although not without controversy,²⁴ that section 19(c) supports the Commission's power to mandate self regulatory organization rules relating to voting rights.²⁵ Professor Karmel further supports this position by iterating to the history of self-regulatory involvement in assuring shareholder suffrage.²⁶

We are currently operating in an environment that has been skewed by the market for corporate control. Takeover activity, both real and rumored, has helped fuel an unknown degree of volatility in the markets. While takeover speculation creates significant upward pressure on stock prices, management entrenchment tactics,²⁷ including but not limited to the creation of disparate voting rights, can push prices in the opposite direction with equal force.²⁸

20. *Id.*

21. *Id.* at 814.

22. *Id.* at 831.

23. 15 U.S.C. § 78s(c) (1982).

24. *See, e.g.,* Dent, *supra* note 14, at 726-27.

25. *See* Karmel, *supra* note 7, at 829; Seligman, *supra* note 14, at 714-19.

26. Karmel, *supra* note 7, at 829.

27. *Stock Prices are Decreased by Poison Pills in Some Cases, SEC Staff Says*, 18 Sec. Reg. & L. Rep. (BNA) 348 (Mar. 14, 1986). *But see Study Shows Fair Price Amendments Have Little Effect on Stock Value*, 17 Sec. Reg. & L. Rep. (BNA) 1829 (Oct. 18, 1985).

28. The issuance of high voting stock is just one of many defensive tactics used by managements to entrench themselves when faced with an anticipated, threatened, or pending takeover attempt. Other tactics include the use of fair price amendments, poison pills, golden parachutes, greenmail, and charter provisions calling for high voting thresholds for hostile mergers. *See generally* A. FLEISCHER, *TENDER OFFERS: DEFENSES, RESPONSES, AND PLANNING* (2d ed. 1983 & 1985 Supp.); T. HAZEN, *supra* note 4, § 11.20; R. WINTER, M. STUMPF & G. HAWKINS, *SHARK REPELLENTS AND GOLDEN PARACHUTES: A HANDBOOK FOR THE PRACTITIONER* (1983); Easterbrook & Fischel, *The Proper Role of a Target's Management in*

While one group of academics maintains that the SEC should adopt a hands-off policy and let the market control,²⁹ public sentiment appears to be to the contrary. It has been argued persuasively that the regulation of management entrenchment tactics should be left to state law in its definition of management duties of care and loyalty. However, the SEC³⁰ proposed federal legislation,³¹ as well as a number of commentators,³² recognize that the climate surrounding the market for control of the country's public corporations is an issue of national significance deserving uniform attention at the federal level. Although, as Professor Karmel notes, the SEC should proceed with caution and reluctance before imposing substantive regulation on voting rights, the failure of the self regulatory organizations to take appropriate corrective action should provide an impetus to the SEC to prevent public corporations from entrenching existing management at the expense of disenfranchising shareholders.

II. COX AND MICHAEL ON INTERNATIONALIZATION OF THE SECURITIES MARKETS

Commissioner Cox and Mr. Michael examine the development of international trading markets for securities and commodity futures that have taken place over the past several years.³³ There are two basic types of linkages that have been used to tie together markets in different nations. One method is to provide for a linkage that allows participants in one market to communicate with their counterparts in another market.³⁴ This can involve both the automatic routing of orders to the most favorable market, and the auto-

Responding to a Tender Offer, 94 HARV. L. REV. 1161 (1981); Lipton, *Takeover Bids in the Target's Boardroom*, 35 BUS. LAW. 101 (1979); Lipton & Brownstein, *Takeover Responses and Directors' Responsibilities—An Update*, 40 BUS. LAW. 1403 (1985); Warden, *The Boardroom as a War Room: The Real World Applications of the Duty of Care and the Duty of Loyalty*, 40 BUS. LAW. 1431 (1985).

29. See Macey & McChesney, *A Theoretical Analysis of Corporate Greenmail*, 95 YALE L.J. 13 (1985) (arguing that greenmail is beneficial for the market); Note, *Greenmail: Targeted Stock Repurchases and the Management-Entrenchment Hypothesis*, 98 HARV. L. REV. 1045 (1985); cf. Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 STAN. L. REV. 819 (1981).

30. See 17 C.F.R. § 240.13e-4(f)(8)(i) (1987) (prohibiting exclusionary self-tender offers).

31. See, e.g., *Congress Responds to Hostile Tender Offers*, 6 BUS. LAW. UPDATE, Sept./Oct. 1985, at 1; see also IRC §§ 280G(b)-(c), 4999 (1986) (imposing excise tax on receipt of golden parachutes and making them nondeductible to the paying corporation).

32. See, e.g., Fiflis, *Of Lollipops and Law—A Proposal for a National Policy Concerning Tender Offer Defenses*, 19 U.C. DAVIS L. REV. 303 (1986); Note, *Controlling Imprudent Lock-Ups: The Necessity for Federal Legislation*, 63 WASH. U.L.Q. 91 (1985).

33. Cox & Michael, *The Market for Markets: Development of International Securities and Commodities Trading*, 36 CATH. U.L. REV. 833 (1987).

34. See *id.* at 836.

matic execution of all such transactions. The Intermarket Trading System (ITS) was the first of such systems and has been implemented pursuant to SEC approval.³⁵ The ITS was viewed as a prototype for trading links and, as approved by the SEC, was premised on automatic routing of orders while retaining broker discretion by not providing for automatic transaction execution.

The ITS is described as primitive since it links brokers and dealers with one another rather than providing a link directly between the markets as is the case with the three securities trading links currently existing between various exchanges.³⁶ These links are regulated through a system of market surveillance and oversight much like the system governing domestic markets. The other type of linkage simply involves the sharing of information about quotations and trades taking place on each of the participating markets. The one current example of such a link is that between the International Stock Exchange of the United Kingdom and the National Association of Securities Dealers' Automated Quotation System.³⁷

According to the evidence analyzed by Commissioner Cox and Mr. Michael, the international trading linkages that currently exist cannot be economically justified in light of the contemporary market environment. The authors maintain that there is insufficient use of the linkages between the markets of different nations to make them cost-effective at present trading levels. Furthermore, based on the level of current usage, there is no indication that linking international markets will increase market efficiency. What then, is the basis for the current move toward internationalization? It appears that the markets are preparing for the needs of the future when projected increases in international transactions will make the trading links and information links between markets more cost-effective.

After analyzing the economic basis for internationalization, Commissioner Cox and Mr. Michael examine the type of regulation that is appropriate. Some commentators have suggested that regulation of international trading will hamper market efficiency.³⁸ However, Commissioner Cox and Mr. Michael disagree, asserting that some degree of regulation is necessary. They conclude that "[i]f there is to be any expansion or modification of trading or operations on linked exchange markets, there must be a base of effec-

35. See Exchange Act Release No. 19,456, 48 Fed. Reg. 4938 (Feb. 3, 1983); see, e.g., Exchange Act Release No. 21,958 (April 18, 1985).

36. See Cox & Michael, *supra* note 33, at 847-48. In addition, there is a link between commodities markets. See *id.* at 853-55.

37. *Id.* at 840.

38. See *id.* at 859-60 n.164 (citation of authorities).

tive surveillance and oversight.”³⁹ Although surveillance of international markets does provide additional costs to the maintenance of international markets, the costs seem justified. As the authors ably point out, international links fail their purpose if they do not operate smoothly. Surveillance and oversight assures the smooth operation of the markets and thus is a cost that is justified by the ensuing integrity and efficiency of the marketplace.

III. CARNEY ON INSIDER TRADING

In his thought provoking article on insider trading, Professor Carney proposes that the increased emphasis on the regulation of insider trading is not warranted.⁴⁰ Professor Carney concludes that little harm can be demonstrated, in general, to either investors or to markets.⁴¹ Professor Carney bases his thesis on the efficient capital market hypothesis and those studies tending to support the hypothesis. The article points to empirical evidence to support the conclusion that insider trading does not lure outsiders into the market. Professor Carney further relies on economic writings that tend to show that insider trading does not significantly affect the market price of stocks.

Based on this evidence, Professor Carney concludes that the absence of a causal connection between insider trading and the inducement of outsider trading precludes a justifiable basis for finding an injury to investors resulting from the profit of insiders who trade on material nonpublic information. Professor Carney further suggests that the absence of any evidence of investor injury means that even the SEC has little if any justifiable basis for regulating insider trading. In fact, he indicates that the Commission’s motivation for aggressive insider trading enforcement is “bureaucratic budget maximization”⁴² in an attempt to take advantage of the projected congressional hearings.

It is undeniable that a direct causal connection cannot be shown between insider trading and investor injury in the context of open market transactions. This realization has led some courts to hold that rule 10b-5 cannot support an implied remedy for investors against insider trading in the open market.⁴³ However, as Professor Carney acknowledges, the courts have not taken what he views as the next logical step. The courts have refused to hold that rule 10b-5 cannot support either SEC enforcement action or criminal

39. *Id.* at 860.

40. Carney, *Signalling and Causation in Insider Trading*, 36 CATH. U.L. REV. 863 (1987).

41. *Id.*

42. *Id.* at 898.

43. *Fridrich v. Bradford*, 542 F.2d 307 (6th Cir. 1976), *cert. denied*, 429 U.S. 1053 (1977); *cf. Moss v. Morgan Stanley, Inc.*, 719 F.2d 5 (2d Cir. 1983), *cert. denied*, 465 U.S. 1025 (1984).

prosecution.⁴⁴

After concluding that investor injury cannot support prohibitions against insiders trading on nonpublic information, Professor Carney examines alternative rationales for regulating trading by insiders. The primary alternative to the investor injury explanation is the misappropriation theory of insider trading. Under this theory it is reasoned that an insider, or anyone else owing a fiduciary duty to the proprietor of the information, who takes information belonging to someone else and reaps a profit thereby, must disgorge that profit. The misappropriation theory of 10b-5 liability for insider trading has had a growing acceptance in the federal courts, at least within the context of SEC enforcement actions and criminal prosecutions.⁴⁵ The misappropriation basis for disgorgement has a sound footing in the common law⁴⁶ and the Supreme Court will soon be addressing its applicability under federal law.⁴⁷

It is legion in the law of restitution that proof of actual injury is not necessary to sustain an action for misappropriation by an agent or fiduciary.⁴⁸ Notwithstanding the firm footing the misappropriation theory has in common law,⁴⁹ one court has repudiated it⁵⁰ and another has limited it for procedural reasons.⁵¹ Without necessarily rejecting the state law basis for misappropriation of confidential information, Professor Carney questions the SEC's role in "protecting the property rights of investment bankers in confidential information received from issuers."⁵² It is highly doubtful that the SEC, or anyone else for that matter, would advance such a rationale in support of vigorous governmental enforcement of the insider trading

44. Carney, *supra* note 40, at 876.

45. See *United States v. Carpenter*, 791 F.2d 1024 (2d Cir.), *cert. granted*, 107 S. Ct. 666 (1986); *United States v. Newman*, 664 F.2d 12 (2d Cir. 1981), *cert. denied*, 464 U.S. 853 (1983); *cf. Dirks v. SEC*, 463 U.S. 646 (1983) (acknowledging that misappropriation may be a valid theory with regard to insiders and those standing in a fiduciary relation); *Chiarella v. United States*, 445 U.S. 222 (1980).

46. See, e.g., *Brophy v. Cities Service Co.*, 31 Del. Ch. 241, 70 A.2d 5 (1949); *Diamond v. Oreamuno*, 24 N.Y.2d 494, 248 N.E.2d 910, 301 N.Y.S.2d 78 (1969); 3 A. SCOTT, *THE LAW OF TRUSTS* § 505.1 (2d ed. 1939); *RESTATEMENT OF THE LAW OF RESTITUTION* § 190 comment a (1937); see also Hazen, *Corporate Insider Trading: Reawakening the Common Law*, 39 WASH. & LEE L. REV. 845 (1982).

47. *United States v. Carpenter*, 791 F.2d 1024 (2d Cir.), *cert. granted*, 107 S. Ct. 666 (1986).

48. *RESTATEMENT (SECOND) OF AGENCY* § 388 comment c (1957); see e.g., Annotation, *Employer's Right to Earnings or Profits Made by Employee*, 13 A.L.R. 905, 907 (1921).

49. See *supra* note 46.

50. *Freeman v. Decio*, 584 F.2d 186 (7th Cir. 1978).

51. *Schein v. Chasen*, 313 So. 2d 739 (Fla. 1975) (dismissing insider trading suit since actual injury to corporation is a precondition of bringing a successful shareholder derivative action).

52. Carney, *supra* note 40, at 897.

prohibitions.⁵³ The proprietary interest of investment banking firms in the information is the basis for creating a fiduciary duty the breach of which has significant adverse impact on the market's integrity.

However, a far more prevalent justification for insider trading regulation is the inherent unfairness that results from permitting insiders to take unlimited personal advantage of nonpublic information.⁵⁴ Professor Carney dismisses as "anecdotal"⁵⁵ these claims that informational advantage of insiders creates unfairness and undermines investor confidence as well as the integrity of the marketplace. But what about a sense of morality and fair play? Taking Professor Carney's view to an extreme, murder can be viewed as an efficient way to rid society of poverty and unemployment, as was portrayed by Johnathan Swift in his *Modest Proposal*.⁵⁶ There is certainly a significant difference in degree between the immorality of taking another's life, for example, and that of reaping personal profits from nonpublic information gathered while in a fiduciary relationship to another. The point remains, however, that arguments of market efficiency and absence of demonstrable harm to investors or the marketplace⁵⁷ do not address issues of fairness.

The views set forth by Professor Carney have been with us for quite a while⁵⁸ and appear to be gathering support, at least among some academics.⁵⁹ However, there has also been substantial criticism of the view that insider trading should not be regulated.⁶⁰ Furthermore, the prevailing regulatory and judicial view is that insiders take undue advantage of their positions when they profit personally from material nonpublic information.⁶¹

53. Professor Carney also suggests that the SEC may have a hidden agenda of trying to beef up its budget appropriations. See *id.* at 897-98.

54. See, e.g., Brudney, *Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws*, 93 HARV. L. REV. 322 (1979); Schotland, *Unsafe at Any Price: A Reply to Manne, Insider Trading and the Stock Market*, 53 VA. L. REV. 1425 (1967).

55. Carney, *supra* note 40, at 878.

56. See generally J. SWIFT, *A MODEST PROPOSAL* (C. Beaumont ed. 1969).

57. While Professor Carney argues that no such harm exists, he apparently concedes that there nevertheless is harm to the proprietor of the confidential information. Carney, *supra* note 40, at 873-74.

58. See generally H. MANNE, *INSIDER TRADING AND THE STOCK MARKET* (1966).

59. See generally Carney, *supra* note 40.

60. See, e.g., Cox, *Insider Trading and Contracting: A Critical Response to the "Chicago School,"* 1986 DUKE L.J. 628 [hereinafter Cox, *Critical Response*]; Cox, *Insider Trading Regulation and the Production of Information: Theory and Evidence*, 64 WASH. U.L.Q. 475 (1986). Professor Cox effectively questions the four arguments generally advanced in support of the abolition of the restrictions on insider trading: (1) "The 'It's An Empirical Question' Argument;" (2) "The Efficient Stock Price Change Argument;" (3) "The Incentive Compensation Argument;" and (4) "The Licensing Through Contracting Argument." Cox, *Critical Response supra* at 642-59.

61. See T. HAZEN, *supra* note 4, § 13.9.

Although there is considerable debate as to whether rule 10b-5 is the appropriate vehicle for regulation,⁶² there is a very strong move afoot from many constituencies to tighten up the insider trading prohibitions.⁶³

IV. LIPTON ON BROKER-DEALER REGULATION

Professor Lipton describes the scope of federal regulation of securities brokers and dealers.⁶⁴ While broker-dealer regulation has always played an important role within the overall context of the securities laws, developments in the nature of the markets foreshadow increased emphasis in this area.

The continued increase in the daily trading volume in the securities markets takes its toll on the ability of brokerage firms to cope with their day-to-day business. The broker-dealer regulation that Professor Lipton describes is thus likely to have its limits tested over the next several years. The proliferation of the options and financial futures markets has added to the typical broker-dealer repertoire and raised new questions concerning the suitability obligations of the broker-dealer.⁶⁵ In addition, wide swings in the volatility of market prices increase the likelihood that customers will feel that they have been led into the wrong investments by their brokers. It is likely that we will continue to witness an increase in broker-dealer fraud litigation.

Other important broker-dealer developments that are likely to be seen in the future focus on the continued struggle concerning the appropriate role of commercial banks in the stock brokerage and investment banking industries.⁶⁶ Last year Congress adopted the Government Securities Act of 1986.⁶⁷ It will be interesting to follow the degree to which the SEC will get involved in the regulation of government securities dealers, and whether that regulation will more closely follow the pattern of municipal securities dealers or of securities dealers generally.⁶⁸

62. See *United States v. Carpenter*, 791 F.2d 1024 (2d Cir.), cert. granted, 107 S. Ct. 666 (1986); see e.g., Anders, *Cloudy Cases: Insider-Trading Law Leads to an Array of Interpretations*, Wall St. J., Feb. 19, 1987, at 31, col. 4.

63. See, e.g., *April Key Month for Insider Trading, Takeover Hearings*, SEC. WEEK, Mar. 30, 1987, at 4; *Latest Proxmire Letter to Shad Focuses on Profits of Risk Arbitrage Firms*, SEC. WEEK, Feb. 23, 1987, at 3; *A Get-Tough Mood on Insider Trading*, BUS. WEEK, May 28, 1984, at 16 (Business Week/Harris Executive poll).

64. Lipton, *A Primer on Broker-Dealer Registration*, 36 CATH. U.L. REV. 899 (1987).

65. See, e.g., T. HAZEN, *supra* note 4, § 10.7.

66. See generally Lipton, *supra* note 64, at 971-84.

67. Government Securities Act of 1986, Pub. L. No. 99-571, 100 Stat. 3208 (1986) (to be codified at 15 U.S.C. § 78o-5). The new legislation became effective on July 25, 1987.

68. The SEC has adopted its proposed rules for government securities dealer regulation. See *Adoption of Rules Implementing Government Securities Act of 1986*, Exchange Act Release No. 24,372, [Current Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,120 (1987-1988

For all of the foregoing reasons, Professor Lipton's description of broker-dealer regulation highlights an important part of federal securities regulation. The importance of this regulation is frequently underestimated.

Transfer Binder) (Apr. 12, 1987); *SEC Clears Government Securities Regulations: Registration Deadline Looms*, SEC. WEEK, Feb. 23, 1987, at 5.

